

UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF RHODE ISLAND

ROBERT RUSSELL HINRICHS, LOUISA  
H. HAMACHECK, JULIE ANN BEINECKE  
STACKPOLE, and RICHARD HINRICHS  
BEINECKE

Plaintiffs,

v.

Civil Action No. 99-209T

CLARENCE H. GIFFORD, JR.  
Defendant.

**DECISION**

ERNEST C. TORRES, Chief Judge, United States District Court.

Some of the income beneficiaries of an irrevocable inter vivos trust brought this diversity action against the sole trustee alleging that the trustee breached his fiduciary duty by prematurely terminating the trust and distributing all of its assets to the residuary beneficiaries.

Because I find that the trust was terminated improperly, judgment will enter surcharging the trustee and requiring him to restore to the trust the sum of \$8,697,245.

**Background**

This case tells a very sad tale. It is a tale of how avarice and the hostile feelings engendered by a bitter divorce have poisoned the relationships among members of an extended family. It also is a tale of how a decent man with an outstanding record of achievement in business and public service agreed to help a friend and, as a result, at the age of 88 and in failing health, finds

himself in the middle of a bitter dispute that has exposed him to a potentially ruinous financial liability; unfairly impugned his integrity; and destroyed the cordial relationship that he previously enjoyed with the beneficiaries of the trust that he administered. The tragedy is further compounded by the fact that litigation of this case may prove to be an exercise in futility because the plaintiffs seek that money be restored to a trust from which they may never be entitled to receive any distribution.

This case was heard in two stages by the Court sitting without a jury. The first stage of the trial focused on whether the plaintiffs' claims were barred by the statute of limitations. In a bench decision, this Court found that the claim of Robert Hinrichs was barred but that the claims of the remaining plaintiffs were not. Accordingly, the Court dismissed Robert's claim, but scheduled the remaining plaintiffs' claims for a trial on the merits.

The second stage of the trial has been completed and counsel have been afforded an opportunity to submit proposed findings of fact and conclusions of law. After considering counsels' submissions, reviewing the voluminous exhibits admitted into evidence, and evaluating the testimony of the witnesses, my findings and conclusions are as follows.

### **Findings of Fact**

#### **I. The 1962 Trust**

On December 18, 1962, Walter Beinecke, Jr., ("Beinecke") established an irrevocable inter vivos trust (the "1962 Trust" or the "Trust") for the benefit of his then wife Mary Ann Hinrichs Beinecke, Mary Ann's four children from a previous marriage (the "Hinrichs children"<sup>1</sup>), and Beinecke's issue. When the Trust was created, Beinecke had three children: Ann Beinecke Oliver, Barbara Beinecke Spitler, and Deborah Beinecke Beale. A fourth child, Walter Beinecke III, was born in 1963.

Beinecke funded the Trust with \$35,000 in cash and named his close friend, Clarence H. Gifford, Jr., then the president of Rhode Island Hospital Trust National Bank ("Hospital Trust"), as sole Trustee. The Trustee was vested with "absolute discretion" to distribute so much of the trust income as the Trustee determined among Mary Ann, the Hinrichs children and their issue, and Beinecke's issue (collectively, the "income beneficiaries"). The Trustee also was given "absolute discretion" to distribute principal to Mary Ann and to Beinecke's issue (collectively, the "residuary beneficiaries") in such amounts and for such purposes as the Trustee deemed advisable. The Trustee's discretion to distribute income and/or principal included authority to "exclude any one or more of the persons to whom distribution may be made" and to "make distribution in equal or unequal proportions."

---

<sup>1</sup> The Hinrichs children are the plaintiffs in this case. They are Robert Hinrichs, Louisa Hamacheck, Julie Stackpole, and Richard Hinrichs.

The Trust provided that it was to terminate upon the death of the last survivor of Mary Ann, the Hinrichs children and the three Beinecke children who were living when the Trust was established.

Upon termination, the trust principal and any accumulated income were to be distributed among Walter Beinecke's then living issue, in equal shares, per stirpes. At the time the Trust was established Beinecke was a New York resident, and the Trust provided that ". . . in all respects [it] shall be construed and regulated by New York law."

When Beinecke created the Trust, he was a principal in Osceola Corporation, a closely-held corporation that had interests in several businesses and, also, owned real estate on Nantucket. Osceola Corporation, later, was renamed Osceola Operating Corporation ("OOC").

The Trust expressly authorized the Trustee:

- (1) To retain any property transferred to the trust, as long as the Trustee in his absolute discretion shall deem it advisable to do so;
- (2) To invest any funds in any stocks, bonds, or other securities or property, real or personal, notwithstanding that such investments may not be of the character allowed to Trustees by statute or general rules of law, and without any duty to diversify investments, the intention hereof being to give the broadest investment powers and discretion to the Trustee . . . and to invest in and to retain and hold securities of Osceola Corporation, or any corporation successor . . . irrespective of the fact that the Trustee may be a director or an officer or otherwise connected with [Osceola Corporation] . . .

During the period relevant to this case, Beinecke owned all

100 shares of the common voting stock in OOC then issued and outstanding. There were several classes of non-voting preferred stock, the holders of which included individual trusts established by Beinecke's mother for the benefit of the Beinecke children (the "Beinecke children's trusts") and trusts established for the Hinrichs children (the "Hinrichs children's trusts").

Shortly after the 1962 Trust was established, it purchased 900 shares of OOC's non-voting common stock for \$27,000. The remaining \$8,000 with which the Trust had been funded was placed in an account at Hospital Trust.

Since only Beinecke's shares had voting rights, he controlled the corporation and was able to conduct its business without sharing information with the other shareholders. For many years, the business struggled financially and generated no income for the 1962 Trust. In order to keep the business afloat, Beinecke, who also was the trustee of the Beinecke children's trusts, made loans from those trusts to OOC without the Beinecke children's knowledge. Those loans were in the form of promissory notes which, by 1978, totaled approximately \$5.7 million. OOC also borrowed money from Hospital Trust and other banks.

## II. Termination of the 1962 Trust

By the mid-1970s, the Beinecke children and the Hinrichs children had become very dissatisfied with Beinecke's failure to provide them with any information about the family businesses in

which their individual trusts had interests. The Beinecke children's dissatisfaction was intensified by the discovery that their father had loaned money from their individual trusts to OOC.

Information about those loans surfaced when Ann Beinecke Oliver and her husband, Hardy, consulted attorney Roland Hjorth for estate planning advice. After reviewing documents provided to him, Hjorth expressed the opinion that Beinecke had violated his fiduciary duty as trustee of the Beinecke children's trusts by investing trust assets in corporations and partnerships in which he had a personal interest. Hjorth described the investments in OOC as "indefensible" and opined that the Olivers had "a very substantial cause of action against Mr. Beinecke." Pl. Exh. 16. That information, apparently, was communicated to the other Beinecke children; and, although they deny ever intending to actually sue their father, they acknowledge that the possibility of a lawsuit was discussed.

Beinecke learned of those discussions from several sources. In 1975, he was informed by Ann who also told him of the Beinecke children's desire to have a greater say in the operation of the family businesses and to be owners rather than creditors of OOC so that they could participate in any future success that it might enjoy. During that conversation, Beinecke assured Ann that he would take steps to "rectify" matters.

In addition, Roger Markhus, OOC's accountant, told Beinecke

that the possibility of a law suit by the Beinecke children had been raised during discussions between attorney Hjorth, Markhus, and Perry Ashley, OOC's attorney. Furthermore, Hardy Oliver alerted Gifford that the Beinecke children had discussed suing their father, and Gifford said that he would talk to Beinecke.

After his conversation with Ann, Beinecke asked Ashley to explore proposals made by Hjorth that were intended to give the Beinecke children a greater equity interest in OOC. There is no evidence regarding the precise nature of these proposals.

In December of 1977, an unprecedented family meeting was held on Nantucket. The Beinecke and Hinrichs children were in attendance when a presentation was made and documents were distributed describing the various family businesses and the complex manner in which they were organized and capitalized. When that portion of the meeting concluded, Beinecke met, privately, with the Beinecke children.

Eight months later, on August 16, 1978, Gifford distributed all of the OOC stock held by the 1962 Trust to Mary Ann Beinecke and the Beinecke children. Mary Ann received 200 shares of the OOC stock, and the four Beinecke children each received 175 shares. It does not appear that the stock had a great deal of value at that time because OOC was continuing to experience financial difficulties. One year after the stock was distributed, the \$8,000 in cash remaining in the Trust also was distributed to Mary Ann and

the Beinecke children, thereby effectively terminating the Trust.

The Hinrichs children were not consulted or informed about those distributions despite the fact that they were income beneficiaries. In fact, they did not even know that the Trust existed. Moreover, Gifford failed to seek a judicial determination regarding the permissibility of terminating the Trust before its specified termination date.

III. The Reorganization and Sale of OOC

In 1981, OOC still was struggling financially and its outstanding debts, including the \$7.9 million then owed to the Beinecke children's trusts, prevented it from borrowing funds needed to meet operating expenses. Thus, Markhus explained OOC's inability to obtain financing as follows:

- Q. And why were you not successful in obtaining financing?
- A. The loan officers that we talked to indicated that even though they would like to do it, they couldn't assure getting it through their loan committee because of the substantial amount of debt and the character of some of the debt that was evidenced on the balance sheet of the companies.
- Q. What was the character of the debt that concerned them?
- A. A lot of the debt had arisen from loans from trusts that were to the benefit of shareholders of the children of Mr. Beinecke.
- Q. And as a result of that initial discussion, Mr. Markhus, did you . . . take any action?
- A. One of the things that the bankers told us was that we should do something to make the balance sheet look better; get rid of some of the debt; use some other alternatives for how to put them in a better position.

I met with Mr. Hawkins and with Walter Beinecke. And after a lot of discussion, including the possibility of having the trust -- the beneficiaries of the trust sign a waiver essentially acknowledging that the loans were okay, we decided -- I suggested that what they do is do a slight reorganization where they would move the assets of the company to a new corporation and leave some portion of the debt behind that was due to the trust.

Accordingly, a plan of reorganization similar to the one suggested by Markhus was adopted (the "1981 Reorganization Plan"). Under that plan, all of the assets, but none of the debts, of OOC were to be transferred to a newly created corporation called Osceola Investment Company ("OIC"). Unencumbered by OOC's debts, OIC would emerge with a sound balance sheet and an ability to borrow the money that it needed. The plan also called for the shareholders of OOC to exchange their stock for stock in OIC thereby giving them an interest in a debt-free company with enhanced prospects of success.

In order to implement the plan, it was necessary to obtain the Beinecke children's agreement to allow the debt owed to the Beinecke Children's trusts to be "left behind" in OOC, as interest-free loans. However, because Mary Ann also owned OOC common stock that was to be exchanged for OIC stock, the Beinecke children were concerned that leaving that debt behind would subject them to a substantial gift tax liability. Their reluctance to incur that liability was compounded by the fact that Mary Ann and Walter Beinecke were experiencing serious marital difficulties that eventually led to bitter and protracted divorce proceedings.

The Beinecke children's concern was eliminated a few months later when Mary Ann sold her 200 shares of OOC stock to Beinecke and the Beinecke children for \$20,000, leaving them as the owners of all of the corporation's common stock. Shortly thereafter, Beinecke gave to his children the OIC stock attributable to the 40 OOC shares that he had purchased from Mary Ann and the 100 shares that he, himself, had owned. Consequently, the Beinecke children ended up with 1,000 shares of OIC common stock, 900 of which were traceable directly to the OOC shares previously owned by the 1962 Trust.

OIC was reorganized again in 1984 in response to revisions in the tax code (the "1984 Reorganization"). The only significant change in capitalization effected by that reorganization was that each of the Beinecke children's trusts received 250 shares of OIC's voting common stock in return for forgiving the \$7.9 million in debt previously "left behind" in OOC.

In 1986, OIC's assets were sold for \$55,380,000. The portion of the net proceeds attributable to the 900 shares traceable to the OOC shares previously owned by the 1962 Trust was \$12,513,512.<sup>2</sup>

#### IV. The Reasons for Termination

---

<sup>2</sup> The portion of the sale price to which the owners of OIC's 2,000 shares of common stock were entitled was \$28,899,413. Pl. Exh. 60. The selling expenses attributable to those shares were \$1,091,607, leaving a net sale price of \$27,807,806 for the owners of these shares. Pl. Exh. 60. Since nine hundred, or 45%, of those shares were traceable to the OOC shares previously owned by the 1962 Trust, the portion of the net sale price attributable to those 900 shares was \$12,513,512.

The Trustee has presented two conflicting explanations for the early termination. Gifford testified that he felt obliged to distribute the assets because the trust was relatively small, it was not producing any income, and the "beneficiaries" requested distribution. Specifically, his testimony was as follows:

- Q. Now prior to making this distribution, Mr. Gifford, did you have any discussions with Walter Beinecke, Jr. about making a distribution such as you made?
- A. Well, as a settlor of the trust, I'm sure. Now you're going back to 1978. I'm sure I talked to the settlor of the trust about what my position - what my thinking was, what I wanted to do. Now exactly in detail what that is, I don't know. But when a beneficiary asks for assets of a small, nonproducing asset, you sort of have to listen. It's been my experience as a trustee of many trusts.
- Q. And, Mr. Gifford, do you have any recollection of any conversations with any of the beneficiaries of that trust about making a distribution?
- A. Absolutely none, that I remember.
- Q. In your opinion, at the time that you made the distribution of that stock, Mr. Gifford, did it have any value?
- A. . . . In thinking, I suppose - to be truthful, I wasn't concerned about the value of it. The beneficiaries wanted their assets, which I was holding for them. I would be less than prudent if I said, "Get lost. You can't have it." It's been my experience as a trustee for years.

Gifford's counsel, on the other hand, assert that the Trust was terminated in order to facilitate a reorganization of OOC that was necessary to keep the business afloat.

Putting aside, for now, whether either of the proffered reasons would have justified terminating the Trust before its

specified termination date, this Court finds that neither reason provides a complete and accurate account of what prompted the termination.

It is difficult to accept the claim that the Trust was terminated because it was unproductive. When Gifford purchased the OOC stock, he knew that it paid no dividends. Furthermore, the settlor clearly intended that the Trust would own OOC stock, even though it generated no income. Thus, the Trust instrument specifically permitted the Trustee to invest in stocks that "may not be of the character allowed to Trustees by statute or general rules of law," and it expressly authorized the Trustee "to invest and to retain and hold securities of Osceola." It is equally difficult to accept the claim that the Trust was terminated because "the beneficiaries" wanted their money. The Hinrichs children also were beneficiaries and, obviously, distribution of all of the assets to the Beinecke children was not something that they desired.

The second explanation is more credible but tells only part of the story. There is no question that the 1981 Reorganization enabled the business to borrow the money that it needed and that the Beinecke children's agreement to "leave behind" OOC's debts to their individual trusts facilitated that reorganization. Nor is there any question that distribution of the Trust's OOC stock to the Beinecke children provided them with an incentive to leave

those debts behind.

However, this Court finds that the primary reason for terminating the 1962 Trust was to protect Beinecke from potential liability for the improper loans that he made to OOC from the Beinecke children's trusts and that the 1981 Reorganization and the concomitant termination of the 1962 Trust simply provided one method for achieving that objective. The evidence shows that both Beinecke and Gifford knew that the Beinecke children had discussed the possibility of a suit against Beinecke and that Beinecke was seeing ways to appease them. The evidence also shows that the options for dealing with the situation were very limited. The \$7.9 million in loans that OOC owed to the Beinecke children's trusts could have been called at any time,<sup>3</sup> and OOC did not have the funds or the ability to borrow the funds needed to repay them. One option that did exist was satisfying the Beinecke children's desire to convert that debt into an equity interest. To appease his children and protect himself from potential liability, Beinecke instructed Perry Ashley to explore Hjorth's proposals for doing

---

<sup>3</sup> Note I to Touche, Ross & Co.'s report on its examination of OOC's financial statements for the year ending December 31, 1977. (Pl. Exh. 78 at Bates 6046) states:

The company is obligated to trusts in the amount of \$5,667,646.00. Certain of the trust instruments do not contain the power to enter into loan transactions. The loans would have to be considered advances returnable upon the demand of the Trustee or the beneficiary. In those trust instruments which contain the power to lend, the loans could be considered voidable upon challenge by any of the trust beneficiaries as the Trustee, Walter Beinecke, Jr., is a principal and creditor of the Company.

that.

As a part of that effort, Beinecke made the decision to distribute the OOC stock and, then, prevailed on Gifford to carry out his wishes. Thus, during his deposition, Beinecke testified as follows:

Q: Whose idea was it to take the OOC stock out of the December 18, 1962, trust and distribute it? . . .

A: . . . I suspect it was my idea.

Q: Whom did you first mention it to?

A: I am not sure whether I would have mentioned it to counsel then to Gifford or vice versa; I think the other way around.

Pl. Exh. 74, p. 100 line 12 - p. 101 line 11.

The absence of any other plausible reason for terminating the Trust, and the irregular and covert manner in which it was terminated, provide further evidence that the purpose of termination was to protect Beinecke. There is no indication that the Beinecke children had any special needs that would have justified early termination or that consideration was given to whether the Hinrichs children had any needs that might weigh in favor of continuing the Trust. In fact, Gifford testified that he did not "give a darn" what the financial circumstances of the Hinrichs children were. While these words undoubtedly reflect the engagingly colorful and sometimes hyperbolic way in which Gifford expresses himself, rather than any indifference on his part to the welfare of the Hinrichs children, they appear to confirm that

termination was not viewed as being in the interest of the Hinrichs children.

In addition, as already noted, the Trust was terminated without notifying the Hinrichs children or seeking judicial approval of the termination. The failure to take those steps, especially by someone with Gifford's considerable trust experience, was highly unusual and strongly suggests that termination was prompted by something more than a desire to enable the business to survive.

### **Conclusions of Law**

#### **I. Fiduciary Duty, in General**

The 1962 Trust expressly states that "in all respects [it] shall be construed and regulated by New York law." Consequently, in deciding whether the Trustee breached any fiduciary duty by terminating the Trust and distributing its assets to the residuary beneficiaries, the Court must apply New York law.

Under New York law, in order to prevail on a claim for breach of fiduciary duty, a trust beneficiary must show that such a duty existed, that it was breached, and that the breach caused some harm to the beneficiary. See O'Hearn v. Bodyonics, Ltd., 22 F. Supp. 2d 7, 12 (E.D.N.Y. 1998); Cramer v. Devon Group, Inc., 774 F. Supp. 176, 184 (S.D.N.Y. 1991).

A trustee has a fiduciary duty to carry out the settlor's intent as expressed in the trust instrument and to act solely in

the beneficiaries' interests. See Restatement (Second) of Trusts § 170; Bogert, Trusts & Trustees § 543, at 217 (2d ed. rev. 1993). The trustee may not act for the purpose of advancing his own interests or those of a third party. See Restatement § 187 cmt. g.

The obligation to act in the beneficiaries' interests requires the trustee to deal impartially with all of the beneficiaries and precludes the trustee from arbitrarily favoring one group of beneficiaries over another group. See Redfield v. Critchley, 300 N.Y.S. 305, 310 (N.Y. App. Div. 1937); Zim Israel Navigation Co. v. 3-D Imports, Inc., 29 F. Supp. 2d 186, 192 (S.D.N.Y. 1998); Restatement § 183 ("Where there are two or more beneficiaries of a trust, the trustee is under a duty to deal impartially with them."). Failure to discharge these obligations constitutes a breach of trust for which the trustee may be held liable. See Estate of Rothko, 379 N.Y.S.2d 923, 940 (N.Y. Surr. Ct. 1975); In re Bruches, 415 N.Y.S.2d at 667-68; Restatement §§ 170 cmt. q & 201; Bogert § 543, at 217.

When the trust instrument vests the trustee with broad discretion to make decisions regarding the distribution of trust assets, the trustee is insulated from liability for good faith judgments in reaching those decisions. See Restatement § 187 & cmt. e. In such cases, a court, generally, should not substitute its judgment for that of the trustee. Id. However, even a provision conferring "absolute discretion" on the trustee does not

relieve the trustee of his fiduciary obligations. In re Chusis, 301 N.Y.S.2d 766, 771 (N.Y. Surr. Ct. 1969). The trustee still is required to deal impartially with the beneficiaries and to act reasonably and in good faith in attempting to carry out the terms of the trust, see In re Application of the Community Service Society, 713 N.Y.S.2d 712, 719 (N.Y. App. Div. 2000), and the trustee may be liable for an abuse of discretion. See In re Bruches, 415 N.Y.S.2d 664, 667-68 (N.Y. App. Div. 1979).

In this case, the Hinrichs children claim that Gifford abused his discretion and breached his fiduciary duty to them by distributing all of the assets prior to the termination date specified in the Trust instrument. Furthermore, they claim that he did so in order to further his own interests and those of Beinecke and the Beinecke children rather than the interests of all of the beneficiaries.

## II. The Justification for Termination

As already noted, the 1962 Trust provided that it would terminate upon the death of the last survivor of Mary Ann Beinecke, the Beinecke children who were living at the time the Trust was established, and the Hinrichs children ("the termination date"). By distributing all of the Trust assets in 1978 and 1979, Gifford, effectively, terminated the Trust before that time, thereby prematurely extinguishing the Hinrichs children's interest as income beneficiaries.

The general rule is that a trustee may not terminate a trust before its specified termination date unless all of the beneficiaries consent. Restatement § 340; Scott On Trusts § 340, at 2708 (3d ed. 1967). Accordingly, if a trust provides for income to be payable to one beneficiary for life and for principal to be payable to another beneficiary after the income beneficiary dies, the trust cannot be terminated without the consent of both beneficiaries. Scott § 337.1, at 2658-61.

Like most general rules, this one has exceptions, but those exceptions are rather limited. Thus, a trustee may be permitted to terminate a trust prior to its specified termination date if changed circumstances make it impossible to achieve the trust's stated purpose; if the trust is so small that the principal will be consumed by the costs of continuing to administer it; or if an otherwise proper distribution exhausts the trust principal. Bogert § 1002, at 341-42, 351. Otherwise, the trustee ordinarily lacks authority to terminate an irrevocable trust prior to its specified termination date.

In any event, even when grounds for termination exist, the trustee ordinarily is required to seek judicial approval of the termination. See Bogert § 992, at 228-29 (absent explicit authorization, trustee has no unilateral power to modify terms of trust, but may petition court for approval); see also In re Estate of Verity, 363 N.Y.S.2d 341, 344 (N.Y. App. Div. 1975) (requiring

hearing to determine whether trust should be terminated on ground that its assets consisted of stock in closely held corporation which had not produced income for twenty years).

In this case, no valid reason has been established for terminating the 1962 Trust. There is no indication that continuing the Trust would have occasioned expenses that threatened to consume the Trust's principal. On the contrary, the evidence shows that Gifford received no compensation for his services as Trustee, and there is no evidence that the Trust incurred any other administrative expenses.

Moreover, the fact that the Trust was not generating any income did not represent any change in circumstances because the Trust had not generated any income since its inception. Nor did that fact make it impossible to achieve the Trust's purpose of providing a potential source of income for the Beinecke children and/or the Hinrichs children during their lifetimes. As subsequent events demonstrated, the possibility still existed that OOC's fortunes would improve and that income might have been available to provide for the Hinrichs children in the future. By distributing all of the Trust's assets, the Trustee foreclosed that possibility and actually prevented achievement of one of the Trust's purposes.

In addition, no justification has been presented for distributing all of the Trust's assets to Mary Ann Beinecke and the Beinecke children. As previously stated, there is no evidence that

any of them had any needs warranting such a distribution. Furthermore, Gifford acknowledged that the decision was made without considering any countervailing needs by the Hinrichs children.

Finally, the lack of any legitimate reason for terminating the Trust before its specified termination date is underscored by the Trustee's failure to seek judicial approval or to notify the Hinrichs children of the proposed termination.

### III. The Motive for Termination

The decision to prematurely terminate the 1962 Trust without sufficient justification is further tainted by the apparent motive for doing so. The Hinrichs children assert that the decision was prompted by a combination of self-interest on the part of the Trustee, a desire to protect Beinecke from potential liability, and an intent to favor the Beinecke children.

#### A. Conflict of Interest

This Court finds no basis for the allegation that Gifford derived any personal benefit from terminating the Trust or that he had any conflict of interest. Evidence that OOC had outstanding loans from Hospital Trust; that Gifford's daughter was a tenant in a building owned by OOC; and that Gifford's son was an architect who once had been employed to design a building for OOC, fall far short of supporting that allegation.

The Hinrichs children ask this Court to infer from these

disparate facts that Gifford had an incentive to terminate the Trust because it would facilitate the reorganization of OOC which, in turn, would prevent the business from failing which, in turn, would enable OOC to pay off its loans to Hospital Trust, continue renting space to Gifford's daughter, and retain Gifford's son for any future architectural services that it might require. However, there is no basis for such an attenuated series of inferential leaps. There is no evidence that, at the time the Trust was terminated, OOC's loan from Hospital Trust was in jeopardy or that Gifford had any personal interest in insuring that it was repaid. In fact, Gifford no longer was employed by Hospital Trust, and he no longer was an active member of the bank's board of directors. Nor is there any indication that Gifford's daughter would have been unable to continue renting from another lessor or, otherwise, would have been adversely affected if OOC failed. There is a similar lack of evidence that Gifford's son had any prospect of providing future services to OOC that would be jeopardized by OOC's failure.

In short, there is absolutely no substance to the claim that Gifford was motivated by self-interest or that he had any personal interests that conflicted with his responsibilities as Trustee.

B. Protection of Walter Beinecke

As already stated, the evidence does support the claim that Gifford terminated the trust, primarily in order to shield Beinecke

from liability for the improper loans that Beinecke had made to OOC from the Beinecke children's trusts. Certainly Gifford's desire to protect his friend and to help the Beinecke family's business was understandable, especially in light of the fact that the contemplated reorganization was likely to benefit the family business in which both the Beinecke and Hinrichs children held a stake. However, by terminating the Trust and distributing all of its assets to Mary Ann and the Beinecke children, Gifford breached his fiduciary duty to act solely in the interest of the beneficiaries and not to favor one group of beneficiaries at the expense of another.

#### IV. The Remedy

##### A. The General Principles

When a trustee wrongfully distributes trust assets, the beneficiaries who are adversely affected may elect to pursue any one of several remedies. They may seek to require the trustee to restore the assets; they may seek to surcharge the trustee for the amount of their loss; or, they may seek to recover the assets from the transferee.<sup>4</sup> See Bogert § 862 & n.4, at 36; see also In re San Juan Hotel Corp., 847 F.2d 931, 938 (1st Cir. 1988) (holding that the general measure of trustee's liability for breach of trust is amount of loss or harm attributable to breach).

---

<sup>4</sup> When the beneficiaries elect to proceed against the trustee, the trustee, in turn, may seek to recover the assets from the party to whom they were transferred. Bogert § 862 & n.4, at 36.

\_\_\_\_\_The ultimate objective is to place the aggrieved beneficiaries in the position that they would have occupied if the breach had not occurred. See Restatement § 205 cmt. a. In this case, the Hinrichs children seek a judgment requiring Gifford "to restore to the Trust any Trust property unlawfully removed therefrom," and "surcharg[ing] the Trustee for any loss of Trust property or income resulting from any breach of fiduciary duty."

B. Causation

Gifford contends that, even if he improperly terminated the Trust, termination did not cause any loss to the Hinrichs children. He argues that if the OOC stock had not been distributed to the Beinecke children, they would not have agreed to "leave behind" the debt to their individual trusts and, as a result, OOC could not have been reorganized and would have failed. There are several flaws in that argument.

First, while it is clear that the reorganization significantly improved the company's fortunes, there is no evidence that, but for the reorganization, OOC would have failed. Indeed, it appears that the subsequent increase in the value of the business was due largely to the boom in Nantucket real estate market.

Second, even if the reorganization was necessary to insure the survival of OOC's business, Markhus acknowledged that it could have been accomplished without terminating the Trust. While termination of the Trust may have provided the Beinecke children with an

incentive for agreeing to "leave behind" the debt owed by OOC, it was not a sine qua non to reorganization.

Finally, there is no indication that reorganization was the only way in which banks could be induced to loan needed funds to OOC. No explanation been offered as to why the banks' reported concern about the outstanding loans to the Beinecke children's trust could not have been addressed in some other way such as subordination of that debt to any loans made by the banks.

C. Damages

In order to recover damages for breach of trust, a plaintiff must prove the amount of the loss caused by the breach with a reasonable degree of certainty and particularity. A remote possibility that the breach might result in future damages and/or mere speculation regarding the extent of the anticipated loss are not sufficient. James Wood Gen. Trading Establishment v. Coe, 297 F.2d 651, 658 (2d Cir. 1961).

Here, the Hinrichs children are unable to establish any quantifiable loss resulting from the early termination of the 1962 Trust. Since the Trustee had absolute discretion to accumulate any income earned by the Trust or to distribute all or any part of it to the income beneficiaries in whatever amounts he determined, the Hinrichs children cannot show that they have been deprived of any income payments to which they were entitled. Cf. James Wood Gen. Trading Establishment, 297 F.2d at 658 (holding that where

stockbroker given discretion to sell stock once it reached certain price and broker failed to sell, customer cannot recover damages because "there is no evidence from which it can reasonably be determined how such discretion will be exercised").

D. Restoration of Principal

The Hinrichs children's inability to prove any quantifiable loss does not leave them without a remedy. As income beneficiaries, they had a legally recognized interest in the Trust. The fact that the value of that interest could not be calculated because it was contingent upon factors such as the Trustee's discretion did not negate that interest. See Restatement § 129 ("The extent of the interest of the beneficiary need not be definite at the time of the creation of the trust. . . .") & cmt. d ("The extent of the interest of the beneficiary may rest wholly within the discretion of the trustee or some third person.") & illus. 7 ("A bequeaths \$100,000 to B in trust to apply the income for the benefit of C or of C's wife and children, D having discretion to determine how much, if anything, should be paid for the benefit of any one of the beneficiaries. C's interest, although contingent as to its extent, is valid.").

Gifford had no authority to extinguish that interest by prematurely terminating the Trust without the Hinrichs children's consent. See Restatement § 340 (requiring the consent of even a contingent beneficiary to terminate trust before specified

termination date). Moreover, by doing so, Gifford acted contrary to the Trust's stated purpose of providing a potential source of income for the Hinrichs children and the other income beneficiaries during their lifetimes.

Since the 900 shares of OOC stock that were distributed no longer exist, it is impossible to require that they be restored to the Trust. The only way to return the Hinrichs children to the position they would have occupied if the Trust had not been terminated improperly is to require Gifford to put back into the Trust an amount equal to the present value of the Trust's rightful share of the proceeds from the sale of OIC's assets.

The portion of the net proceeds from the 1986 sale of OIC's assets that was traceable to the OOC shares previously owned by the Trust was \$12,513,512.<sup>5</sup> However, part of that sum is attributable to the Beinecke children's agreement to "leave behind" the \$7.9 million debt owed to their individual trusts. That agreement facilitated the 1981 Reorganization that enabled the family business to borrow the funds that helped it to prosper and was, at least, partially responsible for the marked appreciation in OOC's stock during the five years after Mary Ann sold her shares for \$200 per share. Furthermore, by allowing OIC to acquire OOC's assets without assuming any liability for that debt, the agreement presumably increased the consideration received for the OOC shares.

---

<sup>5</sup> See supra note 2.

Thus, it is reasonable to infer that if OIC had been required to assume the \$7.9 million debt, fewer OIC shares would have been exchanged for the Trust's OOC shares.

Because the Beinecke children were solely responsible for part of the value received for the OOC shares; and because they will derive little or no benefit from reviving the Trust; and because they are potentially liable for any amount that Gifford may be required to return to the Trust,<sup>6</sup> it would be inequitable to require Gifford to "restore" to the Trust that portion of the value received for the OOC shares that was created by the Beinecke children. See Dan B. Dobbs, Law of Remedies §§ 2.3(2) at 75, 2.1(1) at 57, & 2.4(1) at 92 (court sits in equity when deciding cases based on trusts and has "high degree of discretion" to "measure, shape, or tailor relief to fit [the court's] view of the balance of equities and hardships"). Accordingly, the Trust's share of the \$12,513,512 in net proceeds from the OIC sale that are traceable to the 900 OOC shares previously owned by the Trust must be reduced by \$7.9 million. The resulting figure of \$4,613,512 must be further reduced to \$3,690,810 to reflect the capital gains tax that the Trust would have incurred.<sup>7</sup>

In order to place the Hinrichs children in a position

---

<sup>6</sup> See supra note 4.

<sup>7</sup> The capital gains tax was determined by reducing the net proceeds of \$4,613,512 by 20%, the amount the capital gains tax which was determined to be applicable at the sale of OIC in 1986, and which was agreed to by the parties. See, e.g., Pl. Exh. 60.

comparable to the position they would occupy if the Trust had not been terminated, the \$3,690,810 must be increased to reflect what it now would amount to if it had been received in 1986. One way of making that determination would be to calculate the net return that would have been generated under similar circumstances by a comparable trust. Another method would be to utilize the time value of money represented by the legal interest rate established under New York law.<sup>8</sup>

Ordinarily, the former method would be preferred and it is the one urged by the Hinrichs children. They presented testimony by F. Malcolm Graff, Jr., a former trust officer for a New York trust company. Mr. Graff made a series of complex calculations regarding the amount of appreciation, income, and expenses that he projected a similar trust would have realized or incurred during the 15 year period in question. Those calculations were based on historical data regarding interest rates and rates of return reported by corporate trustees, as well as numerous assumptions regarding such matters as the nature of the Trust's investments; the rate of turnover of the Trust's assets; the income and capital gains taxes

---

<sup>8</sup> The selection of which of these methods to utilize is within the Court's discretion. See Viutton et Fils S.A. v. Carousel Handbags, 592 F.2d 126, 130 (2d Cir. 1979) ("[T]he district judge, sitting in equity, is vested with wide discretion in fashioning a remedy."); see also Dan B. Dobbs, Law of Remedies §§ 2.3(2) at 75 (court sits in equity when deciding cases based on trusts) & 2.1(1) at 57 (court has "high degree of discretion" in equitable cases) (1993). This includes the discretion to "measure, shape, or tailor relief to fit [the court's] view of the balance of equities and hardships." Id. § 2.4(1) at 92.

that would have been incurred; legal fees; the Trustee's rate of compensation; and the amount of income that would have been distributed. It is not clear whether Mr. Graff factored in other expenses such as brokerage fees or fees charged by investment advisors. Nor is it clear whether Mr. Graff took into account the considerable investment discretion that the 1962 Trust vested in the Trustee. Furthermore, it appears that most of the relatively modest number of individually managed trusts with which Mr. Graff was familiar were substantially larger than \$3.7 million.

This Court finds that Mr. Graff's calculations are too speculative to be reliable and that the 9% legal rate of interest established by New York law should be utilized. See N.Y. C.P.L.R. § 5004; see also N.Y. C.P.L.R. § 5001 ("[I]n an action of an equitable nature, [prejudgment] interest and the rate and date from which it shall be computed shall be in the court's discretion.").

The only remaining question is whether the interest to be awarded should be simple or compound. A court sitting in equity has broad discretion to make that decision. See Bogert § 863 at 71-74; Scott § 207. Ordinarily, only simple interest is assessed against a trustee for a breach of trust. Restatement § 207. Indeed, under New York law, compound interest may be awarded only when the Trustee acts in bad faith. See In the Matter of Reveson, 447 N.Y.S.2d 297, 302 (N.Y. App. Div. 1982).

In this case, Gifford's actions were misguided but were not

the product of bad faith. As already noted, he was motivated by a desire to protect his friend, the settlor, from a threatened law suit and to promote the success of the family business in which all of the beneficiaries had an interest. There is no indication that Gifford acted out of malice toward the Hinrichs children or that he, himself, had anything to gain by prematurely terminating the Trust. In addition, the fact that the Trust permitted principal to be paid only to the Beinecke children provided some justification for Gifford to believe that the Beinecke children were the principal objects of Walter Beinecke's bounty. Therefore, compound interest is not appropriate and the amount that must be restored to the Trust hereby is calculated as follows:

|   |              |
|---|--------------|
| Trust's share of proceeds<br>from 1986 sale of OIC: | \$ 3,690,810 |
| Interest from 1986 to 2001<br>at 9% per annum:      | \$ 4,982,595 |
| Cash distributions in 1979:                         | \$ 8,000     |
| Interest from 1979 to 2001<br>at 9% per annum:      | \$ 15,840    |
| TOTAL   | \$ 8,697,245 |

### **Conclusion**

For all of the foregoing reasons, it is hereby ORDERED that judgment enter in favor of the plaintiffs surcharging Clarence H. Gifford, Jr., in the amount of \$8,697,245.00, which amount shall be restored to the 1962 Trust within 60 days.

ENTER:

---

Ernest C. Torres  
Chief United States District Judge  
Date: \_\_\_\_\_, 2001